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COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, NOVEMBER 19, 1998

APPLICATION OF

PELHAM MANOR WATER
SUPPLY COMPANY, INC.

CASE NO. PUE960129

For a certificate of public
convenience and necessity

FINAL ORDER

On August 16, 1996, Pelham Manor Water Supply Company, Inc. ("Pelham Manor" or the "Company"), filed its initial application requesting a certificate of public convenience and necessity to provide water services to the Pelham Manor Estates subdivision located in Culpeper County, Virginia. The Company subsequently raised the issue of whether it was subject to the Commission's jurisdiction or whether it was exempt from regulation pursuant to the "grandfathering" exemption detailed in § 13.1-620 G.¹

In an Order entered on March 26, 1997, the Commission determined that the Company was subject to the Commission's jurisdiction and directed the Company to proceed with its application for certification. By order entered on February 9, 1998, the Commission granted Staff's motion for hearing;

¹ Section 13.1-620 G provides an exemption for a "water or sewer company incorporated before and operating a water or sewer system on January 1, 1970."

appointed a Hearing Examiner; and established a procedural schedule for this case.

A hearing was held on June 3, 1998, before Hearing Examiner, Michael D. Thomas. Marta B. Curtis appeared as counsel for the Commission Staff, and the Company appeared pro se by its president, David K. Travers.

There were several issues in controversy at the hearing. There were accounting issues relating to the recovery of costs associated with the late payment of bills, the payment of federal income tax, and an issue regarding whether it was appropriate to guarantee a dividend to the Company's owner. There were also issues relating to the Company's proposed rules and regulations of service; namely, the appropriate late payment fee and a proposed rule that would prohibit lawn watering, car washing, and pool filling by the Company's customers.

On August 31, 1998, the Hearing Examiner issued his Report. In that Report, the Examiner found that:

(1) The Company should be granted a certificate of public convenience and necessity to provide water service to the Pelham Manor subdivision;

(2) The \$21.00 per month water rate proposed by the Company is just and reasonable;

(3) Staff's disallowance of federal income taxes is proper since the Company, as a Subchapter S corporation, incurs no tax liability as part of its cost of operation;

(4) Staff's accounting and recordkeeping recommendations as detailed in Staff witness Cozad's prefiled testimony appear to be reasonable;

(5) A partial restriction on lawn watering and car washing should be approved. Such restriction would permit lawn watering and car washing prior to 7:30 a.m. and after 7:30 p.m., Monday through Sunday; and

(6) A 1.5% per month late fee is proper.

The Examiner did not address the issue of whether it was appropriate for the Company to have a guaranteed return on rate base. He noted, instead, that the issue that needs to be addressed is whether the Company's revenues generate sufficient cash flow to meet the Company's current and anticipated expenses.

The Examiner recommended that the Commission enter an order that adopts the findings of his Report; issues the Company a certificate of public convenience and necessity; and fixes the Company's rate at \$21.00 per month for residences receiving water service and \$15.00 per month for residences that are connected to the system but are not receiving water service, effective as of July 1, 1996. The Examiner also recommended

that such order require the Company, within sixty (60) days of the Commission's final order in this proceeding, to submit to the Virginia Department of Health ("VDH") plans and specifications to bring its water system into compliance with VDH regulations.

By Order entered on September 15, 1998, the Commission granted the Company's request to extend the date for filing comments on the Hearing Examiner's Report until September 30, 1998. Such comments were filed on September 28, 1998.

In its comments, the Company, among other things, took exception to the Examiner's findings with respect to the recommended water restriction and late payment fee. It was the Company's position that the watering restriction proposed by the Company should be adopted. It was the Company's further position that the \$5.00 late payment fee proposed by the Company should be adopted and that the Commission should initiate an investigation to address the appropriateness of the late fees authorized in its January 10, 1977 Order in Case No. 19589.

NOW THE COMMISSION, having considered the record, the Examiner's Report and the comments thereto, is of the opinion and finds that the Examiner's findings and recommendations should be adopted with the exception of the modifications detailed herein. We will impose no bar or restrictions on water use at this time. The evidence shows that the problem with the

water system is with distribution, not the availability of water. Without a greater showing than presented here, the Company may not impose restrictions on its customers.

In addition to adopting the Examiner's recommendation regarding plans to be submitted to VDH, we will require the Company to submit to the Commission's Division of Energy Regulation a detailed plan regarding a proposed solution that will adequately address the problem of maintaining system reliability. Such plan shall be submitted within 90 days from the date of this Order and shall include, at a minimum, a copy of the engineering specifications and plans submitted to the VDH, the expected cost and date of implementation, financing plans, and the anticipated impact on rates. If the Company is unable to have its plan implemented by next summer, it may petition the Commission for permission to implement reasonable water usage restrictions since usage problems of concern to the Company mostly occur in the summer.

Although the issue of federal income tax was not raised in the Company's comments and exceptions, it was raised at the hearing. We note that, for federal income tax purposes, Pelham Manor is an S Corporation. Therefore, the Company does not have an income tax liability; rather the income of the Company is included in the personal income tax return of the owner. Mr. Travers asserted that cost of service should include a federal

income tax expense allowance for the tax he must pay personally. In 1995, Mr. Travers elected to switch from a C Corporation to an S Corporation, thereby transferring the liability associated with Pelham Manor's taxable income from the corporation to himself. The tax rate differs for an S Corporation compared to a C Corporation, and filing as an S Corporation can provide benefits to the owner. It should also be noted that the decision to switch was Mr. Travers', and he may change his election in the future pursuant to the IRS Code as it suits his circumstances. We agree with the Hearing Examiner and Staff that the tax adjustment requested by Mr. Travers should not be part of the Company's cost of service. Accordingly,

IT IS ORDERED THAT:

(1) The findings and recommendations of the Hearing Examiner, as modified herein, are accepted.

(2) Pelham Manor shall be granted Certificate No. W-292 to provide water service to the Pelham Manor subdivision in Culpeper County, Virginia.

(3) Pelham Manor is hereby authorized to charge its customers \$21.00 per month for residences receiving water service and \$15.00 per month for residences that are connected to the system but not receiving water service, effective July 1, 1996.

(4) Pelham Manor is authorized to charge a 1 ½% per month late payment fee.

(5) Within sixty (60) days from the date of this Order, the Company shall submit to VDH plans and specifications to bring its water system into compliance with VDH regulations.

(6) On or before 90 days from the date of this Order, the Company shall submit to the Commission's Division of Energy Regulation, a plan to address the above referenced service problem. Such plan shall include, at a minimum, a copy of the plans submitted to VDH and the additional details referenced herein.

(7) The Company shall implement Staff's accounting and recordkeeping recommendations.

(8) Within 60 days from the date of this Order, the Company shall file with the Division of Energy Regulation a tariff incorporating the revisions approved herein.

(9) This case is hereby dismissed from the Commission's docket of active cases and the papers placed in the file for ended causes.